



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

TE/GE EO Examinations

1100 Commerce Street

Dallas, Texas 75242

501.07-00

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

Date: 4/09/10

Release Number: **201029038**

Release Date: 7/23/10

LEGEND

ORG = Organization name

XX = Date Address = address

ORG

ADDRESS

Taxpayer Identification Number:

Form:

990 EZ and F-990T

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

**CERTIFIED MAIL – RETURN RECEIPT REQUESTED**

Dear

In a determination letter dated July 19XX, you were held to be exempt from Federal income tax under section 501(c)(7) of the Internal Revenue Code(the Code).

Based on recent information received, we have determined you have not operated in accordance with the provisions of section 501(c)(7) of the Code. Accordingly, your exemption from Federal income tax is revoked effective May 1, 20XX. This is a final adverse determination letter with regard to your status under section 501(c)(7) of the Code.

We previously provided you a report of examination explaining why we believe revocation of your exempt status is necessary. At that time, we informed you of your appeal rights. On September 2, 20XX, you signed Form 6018-A, Consent to Proposed Action, agreeing to the revocation of your exempt status under section 501(c)(7) of the Code.

You have filed Federal income tax returns for the tax period(s) shown above. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United

States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely.

Nanette M. Downing  
Acting Director, EO Examinations

FORM		Schedule or Exhibit No.
886-A	EXPLANATION OF ITEMS	
NAME OF TAXPAYER:		YEAR/PERIOD ENDED
ORG	April 30, 20XX	

LEGEND

ORG = Organization name      XX = Date      Address = address      City = city  
State = state      POA = POA      Co-1, CO-2, CO-3, CO-4, CO-5, CO-6 & CO-7 =  
1<sup>ST</sup>, 2<sup>ND</sup>, 3<sup>RD</sup>, 4<sup>TH</sup>, 5<sup>TH</sup>, 6<sup>TH</sup>, & 7<sup>TH</sup> COMPANIES      RA-1, THRU RA-30 = 1<sup>ST</sup> THRU 30<sup>TH</sup>  
RA

ISSUES: 20XX04

Did organization keep records per Rev Proc. 71-

17? No

Is the net operating loss deductible? No

Is there private benefit/inurement to members? Yes

Is there a substantial non exempt activity from gross income test? Yes

Is revocation warranted? Yes

**Facts:**

Initial interview was conducted with Treasurer, on October 20, 20XX at the club's facility. is the current treasurer of the organization. He provided the following information about the social club.

ORG(ORG) is an organization with a tax exemption per IRC 501(a) as described in IRC 501(c)(7) as a social club. It's membership is limited to 125. It does not actively solicit membership but accepts application.

It operates a facility located at Address, City, State. Its facility is subdivided into two sections. The section that is used on a daily basis is the private club with a gaming room and a bar. The other section is an auditorium or a meeting or multi purpose hall that is rented to members and to the public.

**Private Club:**

The private club is for members only. Members are allowed to bring in guests except on Wednesday nights where weekly membership meeting is held. During Wednesday nights, it provides free dinner to members which does not include drinks such as beer and soda.

The private club has two sections. One section has a billiard table and a card table. It is adjoined to a bar with a lounge and large screen television. Beer is served at \$ each while sodas are at \$ each. They do not serve sandwiches or any other meals.

Members pay the same price as their guests. The guests pay for their own beers and sodas.

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There are usually three bar managers at any given time. The head bar manager handles all the sales proceeds, purchases supplies and other direct expenses, keeps a portion for commissions to himself and pays the sales tax. Each month, the head bar manager, turns over the net proceeds to the Treasurer for around \$ month.

Organization in turn reported the net proceeds as its gross proceeds on its books and F-990 return. Organization did not report funds kept by the bar manager prior to the examination of the return for the following amounts;

Bar Manager	20XX	20XX	20XX	20XX
RA-1	\$ \$	\$ \$	\$ \$	\$ \$

#### Auditorium or multi purpose hall:

The facility has an adjoining auditorium or multi purpose hall. It is leased to members and non members. The lease rate to members is \$ and \$\$ to non members(this was recently increased from \$).

The lease does not cover clean up of the facility.

The rental activity of the auditorium was reported on the F-990T as from unrelated business income with gross receipts of \$\$ and related expenses of \$\$ for a net profit of \$.

This net profit along with investment income of \$\$ was reduced to \$0 unrelated business income before \$ specific deduction by a net operating loss of \$.

The rental activity is managed by RA-2. He handles the bookings, rental receipts, pays expenses and keeps a commission to himself before turning over the net proceeds to the organization.

Organization in turn records the net receipts as its gross rental receipts on its books and records and to the F-990 and F-990T return. Organization did not report funds kept by the rental manager prior to the examination of the return for the following amounts;

Rental manager	20XX	20XX	20XX	20XX
RA-2	\$ \$	\$ \$	\$ \$	\$ \$

#### Additional audit procedures performed

A. REQUESTED ORGANIZATION TO RECONSTRUCT ITS RENTAL INCOME AND EXPENSES PER REV PROC 71-17 AND ACCORDING TO MEMBER AND NON MEMBER INCOME

Organization did not keep adequate books and records. It did not keep records per Rev. Proc 71-17. As noted earlier, it reported revenues net of expenses or commissions or payments made by the lease coordinator and bar managers to themselves.

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**B. REVIEWED ORGANIZATION'S RECONSTRUCTION OF RENTAL INCOME AND EXPENSES AND VERIFIED TO LEASE CONTRACTS AND MEMBERSHIP ROSTER**

Reviewed details of organization's reconstruction of lease revenues and expenses as far as member and non member classification. At the minimum, reconstructed gross revenue is \$ as compared to amount reported on F-990T for \$. However, non member expenses subject to UBI dropped down to \$ but had an increase in net income to \$ as opposed to \$ on F-990T.

Reviewed reclassification and noted that there were revenues classified as membership or rentals but the names of lessees on the contract are not listed on membership roster for 20XX-20XX. That was the only available membership roster provided during the examination. Requested organization to provide documentation to prove membership on IDR#3 for;

- a. RA-3
- b. WW II veterans library

Unfortunately, organization did not provide the requested documentation.

Therefore, the reconstructed revenues and expenses for member and non membership lease of the auditorium were adjusted per examination as follows;

**LEASING ACTIVITY – MEMBER AND NON MEMBER REVENUES AND EXPENSES AS ADJUSTED PER EXAMINATION:**

Reconstructed member & non member use of rental facility							
Rental income per rental contracts		Member	Member	Member	Non member	Non member	Non member
		Revenues	Expense	Net income	Revenue	Expense	Net income
20XX	Rental income - revised						
	May						
	June						
	July						
	August						
	Sept						
	Oct						
	Nov						
	Dec						
	20XX Jan						
	Feb						
	Mar						
	Apr						
	Subtotal						
Quarterly	WWII Veterans Library						
Quarterly	WWII Veterans Library						
Quarterly	WWII Veterans Library						
Quarterly	WWII Veterans Library						
Allocation of Operation exp-P/R							
Total							

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	Operational expense - P/R	
	Ratio of member revenue	
	Ratio of nonmember revenue	84%

Leases reclassified from member to non member for lack of documentation to show that lessees were members of the organization per organization roster of members and as required by Rev. Proc. 71-17 for the following;

RA-3  
RA-4  
RA-5  
RA-6 - CO-1

Other issues:

Organization applied \$\$ of net operating loss from prior years to offset taxable income for fiscal year ending 4/30/20XX.

Copy of the F-990T for FY 4/30/20XX showed it was the originating year of the loss for \$. It had a 75% allocation % for indirect expenses such as utilities, maintenance, depreciation, insurance, supplies, etc.

Organization failed to provide substantiation to show;

- The basis for the allocation % was arrived at to arrive at 75% of indirect costs for the originating year of the net operating loss, and;
- Substantiation for the basis of allocation % used.
- Substantiation for the indirect expenses incurred during the originating year.

In addition, POA has agreed that the net operating loss cannot be substantiated and to forego the deduction.

### **Gross Income Test:**

The gross receipts test requires that;

Gross receipts of IRC 501©(7) organizations should not exceed the following;

- gross receipts from non members use of facility and services including investment income cannot exceed 35% and;
- gross receipts from non members use of facility and services cannot exceed 15%.

ORG did not exercise oversight on the rental revenues handled by the RA-2. The rental manager collected lease revenues and kept commissions and other expenses before turning over the net receipts to ORG treasurer.

Organization in turn recorded the net receipts on its books as its gross rental income and is the amount reported on the F-990 and F-990T returns.

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ORG reconstructed gross rental revenue. The reconstructed gross rental revenue is adjusted per exam for organization's inclusion of some member rental income whose names do not appear on the membership roster and failure to provide substantiation per Rev. Proc. 71-17.

Performed gross income test based upon reconstructed amount of revenue per examination between member and non member rental activity of organization's auditorium. Result of the test is as follows;

	20XX04	Per F-990T return		20XX04	Per Exam Gross revenue	
Per F-990T	UBI	Gross revenue	%	UBI		%
Investment income						
Nonmember income						
Total						

Review of prior year (20XX04) gross income test based on amounts reported on F-990T is as follows;

	20XX04		15/35% test
Per F-990T	UBI	Gross revenues	%
Investment income			3.5%
Nonmember income			25.8%
Total			29.4%

Based upon the above gross receipts test, it appears that the organization did not meet the 15% test for gross receipts from non member use of facility and services in the year under examination for the year ending 4/30/20XX at 31.4%. Prior year return ending 4/30/20XX using the amounts reported on the F-990T return showed its gross income test at 25.8%.

It showed that organization is engaged in more than a substantial amount of non exempt activity.

The findings were presented to the organization and representative. In addition, upon request from the representative, organization was offered an alternative to adopt corrective actions to meet the gross income test and exercise more control over its bar and rental activity.

Organization agreed to the revocation of its tax exemption for failing to satisfy the gross income test. However, when it signed the F-6018, it changed the effective date to May 1, 20XX.

Informed organization that the effective date cannot be changed to a prospective date, it requested that its revocation be reconsidered and will be willing to adopt changes to be in compliance with its exemption requirements. It inquired what steps it needed to adopt to keep its tax exemption;

Per advise of current GM, organization has to adopt the following.



FORM 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No.
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If in case your organization decides to appeal the revocation of tax exempt status with the group manager, at the minimum, the board and officers will have to discuss, vote and adopt changes effective immediately to correct the operation of the organization's activities;

- a. Organization and officers are responsible to ensure that its assets such as cash and investment accounts are being protected. It has to adopt tight internal controls in the operation, cash handling, recording of revenues with all aspects of its activities such as membership fees, rental, bar, golf tournament, and all other fundraising activities.
- b. Organization has to take control of its gross revenues and deposit fully in its bank accounts.
- c. Organization has to pay its expenses by issuing checks and not through cash payouts.
- d. Organization has to deposit fundraising revenues allocated for charitable or community service to a separate bank account from its general fund. It was also noted that organization deposits the net revenue from its golf and other fundraising activities with a number of expenses unaccounted for.
- e. Net operating loss will be disallowed and taxes will be paid on F-990T for the year under audit and subsequent years. It was noted that organization erroneously reported \$ gross revenues on its F-990T for subsequent tax year ending 4/30/20XX.
- f. Bar and rental managers will be under the direct supervision and control of the officers of the organization. There should be complete reporting of revenues and expenses. Expenses should be paid from the bank account and not from cash payouts.
- g. Organization should maintain an inventory of cost of goods sold and purchases related to the bar operations such as drinks, snacks, etc.

POA indicated on 8/17/20XX that organization decided to agree to the revocation of its tax exempt status. It requested 15 additional days to prepare converted F-1120 returns.

The board of directors voted to agree with the proposed revocation on F-6018. It was signed and was received on 8/27/20XX. A copy of the resolution adopted by the board of directors was also provided.

#### **UNRELATED BUSINESS INCOME(UBI) PER IRC 512(a)(3):**

As noted earlier, revenues and expenses from leasing of the auditorium or multi purpose hall to the public or non members were reported on the F-990T on a net of expenses basis.

Reconstruction of member and non member revenues and expenses by the organization were further adjusted for examination purposes per guidelines of Rev. Proc. 71-17 as follows;

#### **LEASING ACTIVITY – REVENUES AND EXPENSES AS ADJUSTED PER EXAMINATION:**

Reconstructed member & non member use of rental facility							
Rental income per rental contracts		Member	Member	Member	Non member	Non member	Non member
				Net			Net
Rental income - revised		Revenues	Expense	income	Revenue	Expense	income
20XX	May						



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June  
 July  
 August  
 Sept  
 Oct  
 Nov  
 Dec  
 20XX Jan  
 Feb  
 Mar  
 Apr  
 Subtotal  
 Quarterly WWII Veterans Library  
 Quarterly WWII Veterans Library  
 Quarterly WWII Veterans Library  
 Quarterly WWII Veterans Library  
 Allocation of Operation exp-P/R  
 Total  
 Operational expense - P/R  
 Ratio of member revenue  
 Ratio of nonmember  
 revenue

20XX04

Rent income  
 Rent expense  
 Net rental income  
 Investment income  
 Net profit on F-990T  
 Net operating loss c/o  
 Unrelated business tax  
 inc.  
 Specific deduction  
 Net taxable income  
 Tax @ 15%

20XX04

20XX04

20XX04

NOL C/O from prior year  
 Ded allowed in current yr  
 C/O to subs year

# **LAW:**

**IRC SEC. 501. EXEMPTION FROM TAX ON CORPORATIONS, CERTAIN TRUSTS, ETC.**

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**501(a) EXEMPTION FROM TAXATION.** —An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503.

**501(c)(7)** Clubs organized for pleasure, recreation, and other nonprofitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder.

#### TAX-REGS, §1.501(c)(7)-1. Social clubs

(a) The exemption provided by section 501(a) for organizations described in section 501(c)(7) applies only to clubs which are organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, but does not apply to any club if any part of its net earnings inures to the benefit of any private shareholder. In general, this exemption extends to social and recreation clubs which are supported solely by membership fees, dues, and assessments. However, a club otherwise entitled to exemption will not be disqualified because it raises revenue from members through the use of club facilities or in connection with club activities.

(b) A club which engages in business, such as making its social and recreational facilities available to the general public or by selling real estate, timber, or other products, is not organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, and is not exempt under section 501(a). Solicitation by advertisement or otherwise for public patronage of its facilities is prima facie evidence that the club is engaging in business and is not being operated exclusively for pleasure, recreation, or social purposes. However, an incidental sale of property will not deprive a club of its exemption. [Reg. §1.501(c)(7)-1.]

#### IRC SEC. 172. NET OPERATING LOSS DEDUCTION.

**172(a) DEDUCTION ALLOWED.** —There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term “net operating loss deduction” means the deduction allowed by this subsection.

#### IRC CODE SEC. 511. IMPOSITION OF TAX ON UNRELATED BUSINESS INCOME OF CHARITABLE, ETC., ORGANIZATIONS.

**511(a) CHARITABLE, ETC., ORGANIZATIONS TAXABLE AT CORPORATION RATES.** —

**511(a)(1) IMPOSITION OF TAX.** —There is hereby imposed for each taxable year on the unrelated business taxable income (as defined in section 512) of every organization described in paragraph (2) a tax computed as provided in section 11. In making such computation for purposes of this section, the term “taxable income” as used in section 11 shall be read as “unrelated business taxable income”.

#### IRC CODE SEC. 512. UNRELATED BUSINESS TAXABLE INCOME.

**512(a) DEFINITION.** —For purposes of this title —

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**512(a)(1) GENERAL RULE.** —Except as otherwise provided in this subsection, the term “unrelated business taxable income” means the gross income derived by any organization from any unrelated trade or business (as defined in section 513) regularly carried on by it, less the deductions allowed by this chapter which are directly connected with the carrying on of such trade or business, both computed with the modifications provided in subsection (b).

**512(a)(3) SPECIAL RULES APPLICABLE TO ORGANIZATIONS DESCRIBED IN PARAGRAPH (7), (9), (17), OR (20) OF SECTION 501(c).** —  
IRC 512(a)(3) –

#### IRC CODE SEC. 513. UNRELATED TRADE OR BUSINESS.

**513(a) GENERAL RULE.** —The term “unrelated trade or business” means, in the case of any organization subject to the tax imposed by section 511, any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501 (or, in the case of an organization described in section 511(a)(2)(B), to the exercise or performance of any purpose or function described in section 501(c)(3)), except that such term does not include any trade or business —

**513(a)(1)** in which substantially all the work in carrying on such trade or business is performed for the organization without compensation; or

**513(a)(3)** which is the selling of merchandise, substantially all of which has been received by the organization as gifts or contributions.

#### IRC CODE SEC. 172. NET OPERATING LOSS DEDUCTION.

**172(a) DEDUCTION ALLOWED.** —There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term “net operating loss deduction” means the deduction allowed by this subsection.

#### Revenue Procedure 71-17 <sup>1</sup>, 1971-1 CB 683

##### SECTION 1. SCOPE AND PURPOSE.

This Revenue Procedure sets forth guidelines for determining the effect gross receipts derived from use of a social club’s facilities by the general public have on the club’s exemption from Federal income tax under section 501(c)(7) of the Internal Revenue Code of 1954. These guidelines will be used in connection with the examination of annual returns on Forms 990 and 990-T filed by social clubs. This Revenue Procedure also describes the records required when nonmembers use a club’s facilities and the circumstances under which a host-guest relationship will be assumed, which are relevant both for purposes of determining adherence to the exemption requirements and for computing exempt function income under section 512(a)(3) of the Code. However, this Revenue Procedure does not deal with other factors bearing on the exempt status of clubs.

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## SEC. 2. BACKGROUND.

.01 *General statement.*--Use of a club's facilities by the general public is significant for two reasons. It may indicate the existence of a nonexempt purpose; or, if not of sufficient substantiality to result in loss of exemption, it may make the club liable for unrelated business income tax. The term "general public" as used in this Revenue Procedure means persons other than members of a club or their dependents or guests. The member's spouse is treated as a member.

.02 *Nonexempt purpose.*--In the examination of information returns of clubs, the problem frequently is to determine under what circumstances and to what extent the fact that a club makes its facilities available to the general public is to be relied upon by the Service as indicating the existence of a nonexempt purpose.

Where a club makes its facilities available to the general public to a substantial degree, the club is not operated exclusively for pleasure, recreation, or other nonprofitable purposes. See Rev. Rul. 60-324, C.B. 1960-2, 173; and Rev. Rul. 69-219, C.B. 1969-1, 153. However, this does not mean that all dealings with the general public are necessarily inconsistent with the club's purposes. See Rev. Rul. 58-589, C.B. 1958-2, 266; Rev. Rul. 68-119, C.B. 1968-1, 268; and Rev. Rul. 69-636, C.B. 1969-2, 126.

.03 *Unrelated business income tax.*--Clubs have been made subject to the tax on unrelated business income for taxable years beginning after December 31, 1969. Section 511(a) of the Code (as amended by the Tax Reform Act of 1969, Public Law 91-172, C.B. 1969-3, 10) and section 512(a)(3) of the Code (added by the Tax Reform Act of 1969).

The unrelated business taxable income of a club is its gross income (excluding any exempt function income), less the allowable deductions directly connected with the production of the gross income (excluding exempt function income), both computed with the modifications specified. Section 512(a)(3)(A) of the Code.

## **TAXPAYER'S POSITION:**

Board of directors adopted a resolution to agree with the revocation of the organization's tax exempt status per IRC 501(c)(7). It signed and submitted a F-6018 which was received on 8/27/20XX.

## **GOVERNMENT'S POSITION:**

### **Recordkeeping requirement per Rev. Proc. 71-71**

Examination of F-990 and F-990T return of ORG(ORG) showed it did not keep records as required by Rev. Proc. 71-17 for social club to show revenues and expenses for member and non member from its rental activity. At the minimum, it warrants an advisory.

## **NET OPERATING LOSS PER IRC 172**

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However, the net operating loss (NOL) that is carried forward to the year under examination is being disallowed per IRC 172 for non substantiation of expenses and basis for allocation of expenses relating to the loss.

The disallowance of the loss will result in tax liability per IRC 511-513. However, this issue is no longer pursued as organization decided to agree with the revocation of its tax exemption status by signing F-6018. Organization will have a F-1120 filing requirement instead of a F-990 and F-990T.

### **REVOCATION OF TAX EXEMPT STATUS PER IRC 501(c)(7)**

Audit procedures performed showed that ORG's tax exemption status warrants a revocation based on the following;

1. Private benefit/inurement to members for funds paid by the rental and bar manager to themselves for operating the bar and rental activity for the following amounts;

Gross Wages	20XX	20XX	20XX	20XX
RA-2	\$ \$	\$ \$	\$ \$	\$ \$
RA-1	\$ \$	\$ \$	\$ \$	\$ \$
Total				

The above funds were not turned over or reported to the organization and operated the rental and bar manager as if it were their own business. These amounts represent net earnings or inurement to the bar and rental manager who are also members of the organization.

2. More than an insubstantial non exempt activity from rental of facilities to non members.

Gross income test showed organization had 31.4% or more than 15% of gross income from its rental of its facility to non members. It is reconstructed as follows;

	20XX04	Per F-990T return		20XX04	Per Exam
	UBI	Gross revenue	%	UBI	Gross revenue
Per F-990T					%
Investment income					
Nonmember income					
Total					

Prior year F-990T (20XX04) was not examined. However, the amounts reported on the F-990T showed gross income test at 25.8% and supports the finding in the year under examination that there is more than an insubstantial non exempt activity from non members as follows;

	20XX04		15/35% test
	UBI	Gross revenues	%
Per F-990T			
Investment income			3.5%
Nonmember income			25.8%
Total			29.4%
			No
			Yes

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The results showed that the organization was not operated exclusively for the benefit of its members and warrants the revocation of its tax exempt status per IRC 501(c)(7).

The proposal for revocation was presented along with an option to adopt changes in its operation to correct deficiencies noted above and operate within the requirements of its tax exempt status.

The board of directors have adopted a resolution dated 8/18/20XX to consent to the revocation of its tax exempt status and signing the F-6018 which was received on 8/27/20XX.

Revocation is effective as of 5/1/20XX and organization agreed to prepare and file converted F-1120 returns.

### **UNRELATED BUSINESS INCOME(UBI) PER IRC 512(a)(3):**

In case the tax exemption status of the organization is revoked for failing to satisfy the gross income test, the F-990 and F-990T returns will be converted to a F-1120 return. Therefore, there is no longer a need to raise the additional tax per IRC 511-513 for UBI on leasing/rental activity of its facility to non members.

However, in the event that organization's tax exempt status is not revoked for whatever reason even though it failed to satisfy the gross income test, an alternative proposal is made for adjustment to non member revenue and expenses which will result in additional tax per IRC 511-513 as follows;

	20XX04		
Rent income			
Rent expense			
Net rental income			
Investment income			
Net profit on F-990T			
Net operating loss c/o			
Unrelated business tax inc.			
Specific deduction per IRC 512(b)(12)			
Net taxable income			
Tax @ 15%			
	20XX04	20XX04	20XX04
NOL C/O from prior year			
Ded allowed in current yr			
C/O to subs year			

Deduction for net operating loss carried over to the year under examination is disallowed in full for \$ for non substantiation per IRC 172 as noted above.



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**CONCLUSION:**

Examination procedures performed showed that ORG did not keep records as required by Rev. 71-17 for social clubs.

Net operating loss carried over from prior years for \$ is being disallowed for non substantiation of expenses and basis for allocation of its expenses from member and non member use of the facility. Disallowance is made per IRC 172.

Examination of ORG's operation, cash handling and recording of the rental and bar activity showed that a portion of the receipts were retained and not turned over by the bar and rental managers. These funds were not reported on the organization's books, F-990, F-990T and payroll returns. The proceeds kept by the rental and bar managers represent inurement/private benefit which is prohibited for organizations exempt per IRC 501(a) as described per IRC 501(c)(7) for social clubs. It warrants a revocation of its tax exempt status per IRC 501(c)(7).

Gross income test performed showed that the revenues from the rental activity of the multipurpose hall to non members greatly exceeded 15% of its gross revenues in the year under examination at 31.4%. Review of F-990T for prior year, which was not audited nor adjusted showed gross income from rental activity greatly exceeded 15% as well at 25.8%. Facts showed that rental activity to non members represent a more than insubstantial amount of non exempt activity as a social organization. It warrants a revocation of its tax exempt status per IRC 501(a) as described per IRC 501(c)(7).

Above findings were presented to organization and its representatives on file. Organization was offered an unagreed conference with Group Manager and to adopt corrective actions.

Organization decided to agree with the proposed revocation of its tax exempt status by signing F-6018 which was received on 8/27/20XX.

Supporting schedule of non member income adjusted per exam for period May 20XX through April 20XX is as follows;

RECONSTRUCTION OF NON MEMBER INCOME PER EXAM							
Rental expenses per tp's reconstruction		Member	Non			Member	Non
		Expense	member	Tot Exp	Revenue	Revenue	Tot Rev
20XX	May		Expense				
5/13/20XX	RA-3-CO-4						
5/20/20XX	RA-7						
5/27/20XX	RA-8						
	Total						
	June						
6/3/20XX	RA-9						
6/11/20XX	RA-9						



FORM   886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No.
NAME OF TAXPAYER: ORG	April 30, 20XX	YEAR/PERIOD ENDED
6/17/20XX	RA-10	
6/24/20XX	RA-11	
	Total	
	July	
7/29/20XX	RA-12	
7/22/20XX	RA-13 #1	
7/15/20XX	RA-14	
7/8/20XX	RA-15	
7/1/20XX	RA-16	
	Total	
	August	
8/6/20XX	RA-3-CO-4	
8/12/20XX	RA-17 & 18	
8/26/20XX	RA-19	
	Total	
	September	
9/9/20XX	RA-20	
9/16/20XX	RA-3/HPC	
9/17/20XX	RA-21	
9/23/20XX	RA-22	
9/30/20XX	CO-2	
	Total	
	October	
10/5/20XX	CO-3 c/o RA-23	
10/6/20XX	RA-4	
10/7/20XX	RA-3-CO-4	
10/14/20XX	RA-24	
10/20/20XX	CO-5 RA-25	
10/21/20XX	RA-26 c/o CO-7	
10/28/20XX	RA-27 c/o RA-28	
	Total	
	November	
11/4/20XX	RA-3	
11/11/20XX	RA-29	
11/25/20XX	RA-30	
	Total	
	December	
12/2/20XX	RA-3-CO-4	
12/7/20XX	CO-1 c/o RA-6	
12/8/20XX	CO-4/ RA-5	
12/9/20XX	RA-3 #1	
12/25/20XX	RA-1	

FORM		Schedule or Exhibit No.
886-A	EXPLANATION OF ITEMS	
NAME OF TAXPAYER:		YEAR/PERIOD ENDED
ORG	April 30, 20XX	

Total

Entity rep for CO-5 is  
RA-7 who is a club member

20XX January  
1/1/20XX CO-7

No rental activity in Jan 20XX but there are deposits to the rental bank account

February  
2/10/20XX RA-18  
2/17/20XX RA-3/ CO-1  
Total

March  
3/3/20XX RA-3/ CO-5  
3/10/20XX RA-22  
3/31/20XX RA-28  
Total

April  
4/28/20XX RA-30  
4/22/20XX RA-12  
4/21/20XX RA-3/ CO-5  
4/14/20XX CO-2